NATIONAL COMMUNITY REINVESTMENT COALITION NCRC

Summary of Testimony of John Taylor
President and CEO,
National Community Reinvestment Coalition

Federal Depository Insurance Corporation Regarding Wal-Mart Bank's Application for Federal Deposit Insurance

Introduction

NCRC is honored to be here today as the voice for our 600 community organizations members representing millions of low- and moderate-income consumers across America. NCRC is the nation's economic justice trade association dedicated to increasing access to credit and capital for minority and working class families.

Over the years, Wal-Mart, the largest retail company in the world, has become the poster child for unscrupulous corporate behavior. It has an abysmal record of low wages and little or no health insurance, as well as a history of civil rights and child labor violations. Now, by trying to become an industrial loan company, Wal-Mart may well add "unsafe and unsound" and "disregard for communities" to its list of abuses. NCRC believes that an ILC of this size would pose significant threats to low- and moderate-income communities, small businesses, community banks, American taxpayers and the U.S. banking system. NCRC does not believe that this application would promote community reinvestment, economic development, nor fair access to reasonably priced credit. Because this would lead to an unhealthy and dangerous combination of banking and commerce, NCRC and its members strongly oppose Wal-Mart's application to establish an industrial loan company. We believe that regulatory agencies should not decide to re-shape entire industries on their own, but must leave these decisions to Congress, the elected body of the public.

While Wal-Mart claims to have limited banking interests, its history of failed attempts to enter the full-service banking industry has shown that it has its eye on the bigger prize. If its application were approved, Wal-Mart would have its foot in the door, making it much easier to expand its financial services down the line.

Banking & Commerce Do Not Mix

Unlike other banks, industrial loan companies fly under the radar of federal regulating agencies. By becoming an ILC, Wal-Mart would be exempt from rigorous regulatory oversight, including safety and soundness examinations which ensure tax-payer deposits are not endangered. Major corporate scandals (like at Enron and Worldcom) highlight the potential financial failures Wal-Mart could similarly engender. If Enron had been an ILC, the U.S. banking system and American taxpayers would be the ones to foot the bill. Now imagine the implications given the massive size of Wal-Mart, which does more business than Target, Sears, Kmart, JC Penney, Safeway & Kroger combined. By approving Wal-Mart's application, regulators would be significantly magnifying an already flawed loophole in the banking system and exposing American taxpayers to great risk.

Mixing banking and commerce imperils safety and soundness because it eliminates the impartiality of the bank. A bank with a commercial affiliate will not base its lending decisions on sound underwriting criteria. Instead, the bank will favor its commercial affiliate and cut-off credit for its competitors. The bank will also be tempted to finance speculative and risky ventures by its commercial affiliate. With a bank the size of Wal-Mart, the end result is significant reduction in credit for independent small businesses and financing for its commercial affiliate, regardless of the riskiness of its activities.

Dodging its CRA Obligations

The Community Reinvestment Act (CRA) was established by Congress as banks were found to have "continuing and affirmative obligations to help meet the credit needs of the local communities in which they are chartered". However, to avoid these solemn legal responsibilities to hard-working community members, Wal-Mart simply tried to skirt its CRA obligations. Within the first few pages of its application, Wal-Mart clearly spells out that low- and moderate-income communities can expect very little from the world's largest corporation that has annual revenues of $290 billion.

While it is now our understanding that Wal-Mart is quickly backpedaling and has reluctantly agreed to abide by CRA, it is doing so only after response to widespread media coverage of their exemption request. Its grudging acceptance of CRA now suggests that Wal-Mart would try to engage in only minimum levels of compliance and reinvestment. This should be a red flag for regulators indicating that Wal-Mart does not take its obligations to communities seriously. This is not the type of corporation that should receive the privilege of a bank charter.

Rather than accepting its obligations to meet the credit needs of its communities in the first place, Wal-Mart initially promised to "serve the needs of the unbanked and underbanked…by participating in financial education programs."[1] While this may be a needed service, education programs alone do not remotely begin to address the needs of the community. If Citigroup or Bank of America attempted to fulfill their community obligations solely through financial education programs, federal regulators and the American public would never tolerate it. Communities need loans for affordable housing, investments in small business development and schools, low-income housing tax credits, grants for community centers, and more. For example, according to its most recent CRA exam in which it received a rating of Outstanding, Merrill Lynch Bank, an existing industrial loan company, made nearly $247 million in community development loan commitments.[2] Because of CRA, traditionally underserved areas that Merrill Lynch serves have access to credit and capital which empowers them to improve their neighborhoods. Wal-Mart, in turn, has an equal responsibility to the communities in which they operate and should not be held to any lower standard.

Wal-Mart Bank would also exacerbate Wal-Mart's current practices of *dis-investing* in communities. Currently, Wal-Mart quickly exports its deposits from local banks, in which the stores are located, to its central headquarters in Arkansas. In addition, as Wal-Mart eliminates its local competitors with below-cost pricing, even fewer deposits are made into local banks. This results in a devastating decrease in the dollars spent in the local area and the credit availability for members of the community, and *pro-actively* weakens communities and diminishes the progress made by CRA.

Wal-Mart should not be quickly absolved for its disregard to communities and federal regulations just because it is now succumbing to pressure from community groups and the public to adhere to CRA.

Wal-Mart's Predatory Pricing Destroys Competition

Initially, the "always low prices" provided by Wal-Mart are appealing to customers and communities. However, Wal-Mart provides below-cost pricing, only to raise prices once competitors have been driven out. Federal courts have even found the pricing to be illegal. By driving down their prices for extended periods of time, Wal-Mart is able to destroy it competition – our small businesses, our small banks, and our communities—and raise prices afterwards. In addition to general merchandise, Wal-Mart Superstores offer full grocery stores, vision centers, auto services, photo processing, dry cleaners, beauty parlors, video rentals and more. Wal-Mart jeopardizes small businesses in all of these areas. For example Wal-Mart opened 60 stores throughout the state of Iowa, where nine NCRC members including a member of our Board of Directors live. Our members watched as they undercut local retailers, building suppliers, drug stores and others because of their market share and ability to offer cheap goods. Thousands of decent paying jobs were lost as a result of massive stores closings. In the end, Wal-Mart entering a community means there will be less product choices available. If this were to occur with banking services, the number of financial service providers would shrink and products would become inflexible and high-cost.

Conclusion

From its poor treatment of employees to its shirking responsibilities, Wal-Mart consistently continues to undermine communities and should not be rewarded for it. If approved, the world's largest retail corporation would be gaining banking privileges that Congress never intended for it to have; it would be given insufficient regulatory oversight due to an exemption from the Bank Holding Company Act; and it would be allowed to meet the bare minimum of its obligations to low- and moderate-income communities under the Community Reinvestment Act. As a result, American taxpayers and the U.S. banking system will be put at risk. The health of community banks, small businesses and the product choices they offer consumers would be jeopardized. On behalf of our 600 member organizations nationwide, NCRC urges the FDIC to reject Wal-Mart's presumptuous application to establish an industrial loan company.

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[1] *Wal-Mart Bank Application*, Industrial Bank Application Package, Utah Department of Financial Institutions, Federal Deposit Insurance Corporation, Volume I of III, p 8.

[2] Merrill Lynch Bank U.S.A., CRA Performance Evaluation, March 31, 2003, p. 10.

NATIONAL COMMUNITY REINVESTMENT COALITION NCRC

Testimony of John Taylor
President and CEO,
National Community Reinvestment Coalition

Before the Federal Depository Insurance Corporation Regarding Wal-Mart Bank's Application for Federal Deposit Insurance

April 10, 2006

Introduction

Good afternoon, my name is John Taylor, and I am President and CEO of the National Community Reinvestment Coalition (NCRC). NCRC is honored to be here today as the voice for our 600 community organizations members representing millions of low- and moderate-income consumers across America. NCRC is the nation's economic justice trade association dedicated to increasing access to credit and capital for minority and working class families. We would like to thank the FDIC for convening these public hearings on an issue that is very important to our members.

Over the years, Wal-Mart, the largest retail company in the world, has become the poster child for unscrupulous corporate behavior. It has an abysmal record of low wages and little or no health insurance, as well as a history of civil rights and child labor violations. Now, by trying to become an industrial loan company, Wal-Mart may well add "unsafe and unsound" and "disregard for communities" to its list of abuses. NCRC believes that an ILC of this size would pose significant threats to low- and moderate-income communities, small businesses, community banks, American taxpayers and the U.S. banking system. NCRC does not believe that this application would promote community reinvestment, economic development, nor fair access to reasonably priced credit. Because this would lead to an unhealthy and dangerous combination of banking and commerce, NCRC and its members strongly oppose Wal-Mart's application to establish an industrial loan company. We believe that regulatory agencies should not decide to re-shape entire industries on their own, but must leave these decisions to Congress, the elected body of the public.

Wal-Mart claims to have limited banking interests as it is promising to only process credit cards, debit cards and electronic check transactions. However, we are more than suspicious of this claim as history has shown that the retail giant has a larger objective in mind. In the past eight years, Wal-Mart has made several attempts to enter into the full-service banking industry – all of which have failed. In 1998 Congress closed a back-door loophole after Wal-Mart attempted to purchase an Oklahoma-based thrift. Three years later, the OTS rejected a partnership Wal-Mart tried to unlawfully maneuver with a Toronto-based bank. Then in 2002, the California legislature passed a law blocking Wal-Mart from purchasing a local industrial loan company.

Wal-Mart is still trying to get its foot in the door of the full-service banking world. If its application is approved, this industrial loan company would process hundreds of million of transactions according to Wal-Mart officials. As such, the ILC would represent a revenue source that would generate billions of dollars. NCRC believes that the strongest firewalls imaginable would not thwart the temptation for Wal-Mart to use loan company revenue to further expand its commercial business. If the FDIC approves this application, it will make it much easier for Wal-Mart to expand into full service banking operations down the line, posing significant safety and soundness dangers.

Banking & Commerce Do Not Mix

By becoming an ILC, federal regulators would be allowing Wal-Mart to have the same privileges of a regular bank without the rigorous regulatory oversight required of them. Unlike other banks, industrial loan companies fly under the radar of federal regulating agencies. ILCs are exempt from the Bank Holding Company Act (BHCA), which requires safety and soundness examinations of banks and their parent company. Without these protections in place, the U.S. banking system and American taxpayers who fund the federal safety net for banks and ILCs are put at serious risk. Major corporate scandals, such as at Enron and Worldcom, highlight the potential financial failures Wal-Mart could similarly engender. If Enron had been an ILC, the U.S. banking system and American taxpayers would be the ones to foot the bill. Now imagine the implications given the massive size of Wal-Mart, which does more business than Target, Sears, Kmart, JC Penney, Safeway and Kroger combined. By approving Wal-Mart's application, regulators would be significantly magnifying an already flawed loophole in the banking system and exposing American taxpayers to great risk.

Mixing banking and commerce imperils safety and soundness because it eliminates the impartiality of the bank. A bank with a commercial affiliate will not base its lending decisions on sound underwriting criteria. Instead, the bank will favor its commercial affiliate and cut-off credit for its competitors. The bank will also be tempted to finance speculative and risky ventures by its commercial affiliate. With a bank the size of Wal-Mart, the end result is significant reduction in credit for independent small businesses and financing for its commercial affiliate, regardless of the riskiness of its activities.

While Wal-Mart would start as a special purpose bank processing credit cards, it will quickly amass a sizable amount of profits and capital. Where would Wal-Mart invest these profits and capital? It is likely these investments would be anti-competitive and also could be risky.

While Wal-Mart may point out that is not alone in its attempt to establish an ILC, this does not rectify the fact that it is exploiting an outdated and already abused loophole. NCRC and other consumer advocate organizations support the complete elimination of the ILC loophole and have petitioned Congress to close the loophole as it considers regulatory relief provisions:[1]

> ILCs were never intended to be large, nationwide banks that offered services indistinguishable from commercial banks. In 1987, Congress granted an exception to the BHCA for ILCs because there were few of them, they were only sporadically chartered in a small number of states, they held very few assets and were limited in the lending and services they offered. In fact, this exception specifically applied only to ILCs chartered in five states (Utah, California, Colorado, Nevada and Minnesota) that have either assets of $100 million or do not offer checking services. Since that time, however, everything about ILCs has grown: the number that exist, the amount of

[1] Testimony Before the Senate Committee on Banking, Housing & Urban Affairs Regarding the Consumer Impact of Regulatory Relief Proposals Affecting Banks, Thrifts, and Credit Unions, March 1, 2006, Presented by: Consumer Federation of America, U.S. Public Interest Research Group, ACORN, Consumers Union and National Community Reinvestment Coalition, and others; p. 19.

> assets and federally insured deposits in them and the services and lending products that they can offer.
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> According to the General Accounting Office (GAO), ILC assets grew by over 3,500 percent between 1987 and 2004, from $3.8 billion to over $140 billion. In 2004, six ILCs were among the 180 largest financial institutions in the country with $3 billion in assets. According to the Federal Reserve, the majority of ILCs had less than $50 million in assets in 1987, with assets at the largest ILC at less than $400 million. As of 2003, one ILC owned by Merrill Lynch had more than $60 billion in assets (and more than $50 billion in federally insured deposits).

It is time to shut down this parallel banking system, not allow its further expansion. The Federal Reserve Board has also recommended that the ILC exemption be eliminated. NCRC and its members strongly urge the FDIC to reject Wal-Mart's application to establish an ILC and call on Congress to close the ILC loophole permanently.

Dodging its CRA Obligations

Passed by Congress in 1977, the Community Reinvestment Act (CRA) states that banks have "continuing and affirmative obligations to help meet the credit needs of the local communities in which they are chartered". The act also established a regulatory regime for monitoring the level of lending, investments, and services in low- and moderate-income neighborhoods that have been traditionally underserved by lending institutions. For special purpose banks, such as industrial loan companies, this might include affordable housing loans, low-income housing tax credits, or investments in organizations that finance small businesses. However, to avoid these solemn legal responsibilities to communities, Wal-Mart simply requested to be exempt, or rather opt out, of its CRA obligations. Within the first few pages of its application, Wal-Mart clearly spells out that low- and moderate-income communities can expect very little from the world's largest corporation that has annual revenues of $290 billion.

While it is now our understanding that Wal-Mart will abide by CRA, it is doing so only after response to widespread media coverage of their exemption request. Despite Wal-Mart's claim of being misguided by its legal counsel[2], the retail giant is only backpedaling now for its own interest, which is to establish a bank. Its grudging acceptance of CRA now suggests that Wal-Mart would try to engage in only minimum levels of compliance and reinvestment. This should be a red flag for regulators indicating that Wal-Mart does not take its obligations to communities seriously. This is not the type of corporation that should receive the privilege of a bank charter.

Under §345.11 of the FDIC's CRA regulation, Wal-Mart claimed an exemption from CRA as a bank not performing ordinary retail services for the general public. However, Wal-Mart will be processing hundreds of millions of credit card payments from its customers. Essentially, Wal-Mart would be participating in granting credit to their customers since it is processing their debt payments. Wal-Mart's attempt to evade CRA responsibilities was particularly audacious since

[2] Marcus Kabel, "Wal-Mart Alters Its Bank Plan", *Associated Press*, March 26, 2006. http://www.philly.com/mld/inquirer/business/14186153.htm?template=contentModules/printstory.jsp

ILCs of comparable size comply with CRA and have executed commendable community development financing activities**.**

Rather than accepting its obligations to meet the credit needs of its communities in the first place, Wal-Mart initially promised to "serve the needs of the unbanked and underbanked residents of the Salt Lake City MSA by participating in financial education programs." [3] While this may be a needed service, education programs alone do not remotely begin to address the needs of the community. Communities need loans for affordable housing, investments in small business development centers and schools, low-income housing tax credits, economic development loans, grants for community centers, funding for Community Development Financial Institutions (CDFIs) and more. If Citigroup or Bank of America attempted to fulfill their community obligations solely through financial education programs, imagine the response of federal regulators and the American public. It would never be tolerated. Regardless of the impact of the programs, financial education would never be able to replace the access to credit and capital which CRA obligates banks to provide.

In contrast to Walmart's intentions, existing industrial loan companies (ILCs) make significant CRA-related loans and investments. For example, according to its most recent CRA exam in which it received a rating of Outstanding, Merrill Lynch Bank, an ILC, made nearly $247 million in community development loan commitments.[4] Of this total, almost $59 million were non-revolving loans including funding for a charter school in a low- and moderate-income neighborhood and loans in affordable housing construction. Merrill Lynch also made over $202 million in qualified investments, which went to venture capital funds for small business investment companies, low-income housing tax credits, and loan pools that provide long-term financing for low- and moderate-income multi-family housing. Without CRA, traditionally underserved and vulnerable communities that Merrill Lynch serves in New York, New Jersey and Utah would not have this access to credit and capital to help them. Wal-Mart, in turn, has an equal responsibility to the communities in which they operate and should not be held to any lower standard.

NCRC is also deeply concerned that a Wal-Mart Bank would exacerbate Wal-Mart's current practices of *dis-investing* in communities. Wal-Mart is already known to quickly export its deposits from local banks, in which the stores are located, to its central headquarters in Arkansas. This results in a devastating decrease in the dollars spent in the local area and the credit availability for members of the community. In addition, as Wal-Mart's eliminates its local competitors with below-cost pricing, even fewer deposits are made into local banks.

CRA was established to ensure that deposits taken from communities were reinvested back into that same neighborhood. Before backpedaling in efforts to save face, Wal-Mart was not only trying to skirt its legal responsibilities to hard-working community members, but it has already been *pro-actively* weakening communities and diminishing the progress made by CRA. Wal-

[3] *Wal-Mart Bank Application*, Industrial Bank Application Package, Utah Department of Financial Institutions, Federal Deposit Insurance Corporation, Volume I of III, p 8.
[4] Merrill Lynch Bank U.S.A., CRA Performance Evaluation, March 31, 2003, p. 10.

Mart should not be quickly absolved for its disregard to communities and federal regulations just because it is now succumbing to pressure from community groups and the public to adhere to CRA. Instead, the FDIC must take this as opportunity to confirm that Wal-Mart will act only when it is in their best interests. The FDIC must take these manipulative and anti-community actions into consideration as it contemplates whether approving Wal-Mart's application would decrease or increase reinvestment in America's communities.

Wal-Mart Already Has an Abysmal Record

While Wal-Mart's request to dodge its CRA obligations is its first direct statement about its future banking relationship with communities, it is not the first time Wal-Mart has abused the members of its communities. Over the years, Wal-Mart has become the poster child for greedy corporate behavior with its low wages, little or no health care, gender and race discrimination suits, and environmental and child labor violations. When banks submit an application to merge, regulators are required to review any violations of anti-discrimination laws or other regulations. If Wal-Mart wants to establish a federally-insured bank, then it must be held to the same standards as other financial institutions. After conducting a thorough review of Wal-Mart's abysmal record of civil rights violations, regulators must reject Wal-Mart's application to establish a bank.

For example, a Wal-Mart sales clerk (the most common position at Wal-Mart)[5] earns on average $8.50 per hour or approximately $14,000 per year, which is below the poverty level for a family of three.[6] Of the 1.25 million U.S. Wal-Mart employees, over half get no health care and those that do get health care have a $1,000 deductible. Paying a $1,000 deductible with an annual salary of $14,000 is practically impossible for most workers. In comparison, Costco pays their workers an average of $16.00 per hour and provides health insurance to 82% of its workers. With low pay and minimal benefits, tens of thousands of Wal-Mart employees must turn to Medicaid, food stamps, housing assistance, federally reduced lunches and low income energy assistance. In fact, Wal-Mart employees were eligible for an estimated $2.5 billion in federal assistance in 2004.[7] As Wal-Mart chooses to offer "always low wages and benefits", American taxpayers are left to subsidize the rest.

Wal-Mart also has the dubious distinction of being subject to the largest class action law suit in U.S. history. Over 1.6 million women have sued Wal-Mart for gender discrimination for denying them promotions and paying them less than men. Women make up 72% of the hourly workforce, but only 33% of Wal-Mart's associate managers and 15% of senior store managers.[8] On average, women at Wal-Mart earn 5-15% less than men. Wal-Mart is also being sued in several states for racial discrimination, environmental violations, and more.

[5] Wakeup Walmart, http://www.wakeupwalmart.com/facts/, March 19, 2006.
[6] Wal-Mart Watch, *Low Prices at What Cost: Annual Report 2005*, p. 7.
[7] Harpers Index, March 2005, http://www.harpers.org/HarpersIndex2005-03.html, March 19, 2006.
[8] Wal-Mart Watch, *Low Prices at What Cost: Annual Report 2005*, p. 16.

Wal-Mart's Predatory Pricing Destroys Competition

Wal-Mart's application states that "the operations of the Bank should not impact the local banking community." [9] Again, however, Wal-Mart's history speaks quite differently. The world's retail giant has been known to drive out competition in almost every industry it has entered. Why should regulators and the public believe that Wal-Mart would have any less of an impact on the banking community?

Initially, the "always low prices" provided by Wal-Mart are appealing and possibly a selling point to customers and communities. However, Wal-Mart provides low cost and even below-cost pricing, only to raise prices once competitors have been driven out. Wal-Mart Watch reports that in 2003, a federal judge banned Wal-Mart from continuing to sell gas below wholesale cost after the court found it lost $300,000 on gas sales.[10] By driving down their prices for extended periods of time, Wal-Mart is able to destroy it competition – our small businesses, our small banks, and our communities—and raise prices afterwards.

In addition to general merchandise such as DVD players and clothing, Wal-Mart Superstores offer full grocery stores, vision centers, auto services, photo processing, dry cleaners, beauty parlors, video rentals and more. Wal-Mart jeopardizes small businesses in all of these areas. For example Wal-Mart opened 60 stores throughout the state of Iowa, where nine NCRC members including a member of our Board of Directors live. Our members watched as they undercut local retailers, building suppliers, drug stores and others because of their market share and ability to offer cheap goods. Thousands of decent paying jobs were lost as a result of massive stores closings, including 555 grocery stores, 298 local hardware stores, 293 building suppliers, 161 variety shops, 150 women's stores and 116 local pharmacies.[11]

In the end, Wal-Mart entering a community means there will be less product choices available. If this were to occur with banking services, the number of financial service providers would shrink and products would become inflexible and high-cost.

Conclusion

Wal-Mart's presumptuous application must be rejected. If approved, the world's largest retail corporation would be gaining banking privileges that Congress never intended for it to have; it would be given insufficient regulatory oversight due to an exemption from the Bank Holding Company Act; and it would be allowed to meet the bare minimum of its obligations to low- and moderate-income communities under the Community Reinvestment Act. As a result, American taxpayers and the U.S. banking system will be put at risk. The health of community banks, small businesses and the product choices they offer consumers would be jeopardized.

[9] *Wal-Mart Bank Application*, Industrial Bank Application Package, Utah Department of Financial Institutions, Federal Deposit Insurance Corporation, Volume I of III, p 8.
[10] Wal-Mart Watch, *Low Prices at What Cost: Annual Report 2005*, p. 4.
[11] Ibid, p. 10.

From its poor treatment of employees to its shirking responsibilities, Wal-Mart consistently continues to undermine communities and should not be rewarded for it. NCRC is deeply concerned about the many negative implications of Wal-Mart's application and does not believe that this application would promote community reinvestment, economic development, nor fair access to reasonably priced credit. On behalf of our 600 member organizations nationwide, NCRC urges the FDIC to reject Wal-Mart's application to establish an industrial loan company.